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STATE FOR EAP/CM

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TAGS: ECON EFIN EINV ETRD MO CH

SUBJECT: MACAU GAMING BOOM THREATENED BY RESTRICTED VISAS,  
SHADY JUNKET OPERATORS, UNDERDEVELOPED INFRASTRUCTURE

REF: HONG KONG 793

Classified By: Consul General Joseph Donovan for reasons 1.4 (b) and (d)  
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¶1. (C) Summary: U.S. casino executives, Macau government officials and gaming industry experts tell us new constraints are harming continued growth in Macau's gaming industry. While gaming has driven Macau's double-digit economic growth in recent years, gaming company executives said the PRC's recently imposed visa restrictions had begun to materially affect revenues: monthly casino revenue fell in September 2008 (compared with the prior year period) for the first time since January 2006. Casino operators regret the growing power of "junket" operators in mainland China that account for most of the Macau casinos' earnings and who, themselves, may have earned USD 2 billion. They believe the operators are directly or indirectly involved with organized crime in Macau and the mainland. Macau's gaming executives criticized Macau's government as unsophisticated, opaque in its decision-making, and hamstrung by a recent corruption scandal. They also cited government interference in the local labor market and insufficient spending on infrastructure projects as impediments to Macau's growth potential. End summary.

¶2. (C) Comment: The Macau "boom" - predicated on billions of dollars in foreign investment and four years of double-digit growth in visitor arrivals - may be sharply slowing. In addition to a global economic slowdown, the fact that mainland gamblers account for the majority of funds flowing into Macau appears increasingly undesirable to Beijing. The perception is widespread that, with the implicit assistance of the big "junket" operators, some of these mainlanders are betting with embezzled state money or proceeds from official corruption, and substantial portions of these funds are flowing on to organized crimes groups in mainland China, if not Macau itself. In this context, Beijing's decision to restrict PRC visitors to Macau has the added benefit (to Beijing) of forcing casino operators to look further afield for customers. In addition, Chief Executive Ho has been hamstrung by a major corruption scandal within his cabinet, and is increasingly seen as a lame duck as he approaches the end of his term in late 2009. Significant decisions will likely remain on hold until his successor takes office. Gaming operators also face a dilemma: whether to continue to massively expand investment as planned, in spite of slowing revenue growth, or to scale back. End comment.

Visa Restrictions Placed on Mainlanders Visiting Macau

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¶3. (C) The PRC government has tightened restrictions on the flow of mainlanders into Macau. Effective September 1, mainland Chinese citizens are precluded from using Hong Kong

as a transit point for visits to Macau, unless they obtain an additional HK-Macau travel permit. In addition, the frequency of direct visits to Macau (i.e., not through Hong Kong) by mainlanders has been substantially reduced through slower processing of visas and tightened permit restrictions by mainland officials. In the four years through 2007, the average annual growth rate of visitor arrivals in Macau exceeded 20 percent. While visitor arrivals grew another 17 percent to 20.2 million individuals during the first eight months of 2008, compared with the same period in 2007, casino executives told us the new visa restrictions imposed by Beijing have reduced both visitors and gaming revenues in September 2008. A senior U.S. executive at Wynn Macau told EconOff recently that Wynn's revenues in September were down approximately 15 percent from the prior year (proprietary information; please protect).

**¶4.** (U) Nine-tenths of Macau's visitors come from mainland China, Hong Kong or Taiwan. According to the Director of Macau's Tourist Office, mainland visitors accounted for 58 percent of all visitors to Macau during the first eight months of 2008. (Note: During the same time period, visitors to Macau originated from other locations as follows: Hong Kong 27 percent, Taiwan 4 percent, with no other source accounting for more than 1.5 percent. End note.) Casino operators are very nervous about the decline in revenues from mainland visitors, as almost all of Macau's gaming companies are implementing expansion plans; the global credit crunch adds to these fears. Investors took notice and hammered the shares of the three U.S. publicly traded gaming companies in Macau. In the 30 days ending October 21, 2008, while the S&P 500 Index fell 21 percent, the share price of Las Vegas Sands

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(LVS) declined 72 percent. Wynn Resorts and MGM Mirage fell 45 percent and 60 percent, respectively.

#### 117 Percent Growth in Hotel Rooms During Next Two Years

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**¶5.** (U) Macau currently has 17,651 hotel rooms and 29 casinos in operation. Against the backdrop of tighter visa restrictions on mainlanders visiting Macau, massive construction projects already underway are scheduled to create eleven new casinos and add 22,000 hotel rooms in Macau during the next two years. Most of those new rooms will be located in sixteen new five-star hotels in and around the "Cotai Strip," a LVS-sponsored development adjacent to LVS' Venetian Resort and Casino, the largest hotel/casino in the world. All of the hotels will be directly linked with new, already licensed casino operations. LVS needs externally sourced funds totaling at least USD 2 billion, in order to complete construction of its portion of the Cotai Strip. However, media reports from October 20 stated LVS has been forced to put a multi-billion dollar syndicated credit facility on hold, due to the global credit crunch and the Macau gaming market's looming supply/demand imbalance. While LVS' largest shareholder, multi-billionaire Sheldon Adelson, could possibly provide the funds needed to complete his company's construction plans, market analysts speculate he would take such action only if Beijing significantly loosened visa restrictions.

**¶6.** (C) With near zero unemployment in Macau (due to increasing market demand and MSARG hiring restrictions on both domestic and foreign workers), casino operators are maintaining padded payrolls - in some cases including thousands of extra workers - to accommodate their future needs. A senior executive for the Stanley Ho Group of gaming companies told EconOff on September 25 that his company currently has "3,000 too many" employees. He said the Ho Group will reduce this excess through attrition and opening two new gaming venues in 2009.

Inadequate Infrastructure, MSARG Corruption and Incompetence

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¶7. (C) Observers offer various theories to explain the PRC's implementation of new visa restrictions at a time of explosive construction growth in Macau. University of Macau Professor of Economics Ricardo Siu (protect) told EconOff that Beijing wants to slow Macau's growth rate, in order to allow the MSARG to build adequate support infrastructure. (Note: Siu is a paid advisor to the MSARG. End note.) He said, "(The MSARG) must slow things down now. It's time to consolidate, in order to ensure sustainable growth." He noted that the (less volatile) non-gaming expenditures by visitors to Macau account for only 10-15 percent of the total, while the portion of non-gaming expenditures by visitors to Las Vegas exceeds 40 percent. In addition to the visa restrictions, he said Beijing has pushed the MSARG to strengthen internal control procedures at the casinos and amend Macau's Gaming Law and regulations. He said the MSARG will soon propose amendments to the Gaming Law and ask the casino operators "behind the scenes" for comments on its proposals.

¶8. (C) Siu said other factors also prompted Beijing's visa restrictions. He cited the January 2008 sentencing of Macau's former Secretary for Transport and Public Works, Ao Man-long, to 27 years in prison for corruption, money laundering, abuse of power and other crimes. Siu said the case was a "wake-up call" for Beijing that prompted increased oversight. He said PRC leaders believe corruption within the MSARG "likely extended well beyond Ao." A lawyer within the Macau government (protect) agreed, telling us that Beijing implemented the visa restrictions as a warning to Chief Executive (CE) Edmund Ho that he had better get his government on track.

¶9. (C) While none of the casino operators would comment directly about corruption within the MSARG, the president of a major U.S. gaming operation in Macau told EconOff that the MSARG "is not very sophisticated." He said, "There is a significant lack of intellectual firepower within the Macau government." Several casino executives told us CE Ho has lost the respect of Beijing and is a "lame duck," following the Ao scandal. As a possible sign of a MSARG leadership vacuum, casino operators pointed to the MSARG's failure in the past several months to make licensing decisions for several pending hotels and bars.

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#### Organized Crime Benefiting from the Boom?

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¶10. (C) Casino gaming accounts for a majority of Macau's approximately USD 18 billion GDP. Despite efforts to grow mass-market gaming in Macau, wealthy gamblers brought into Macau by junket operators accounted for approximately 60-70 percent of Macau's aggregate gaming earnings (or "win") of USD 10.2 billion in 2007. This means that over one third of Macau's economy is effectively controlled by junket operators. The MSARG licenses junket operators, and fewer than a dozen of these dominate the market. They assume each mainland's credit risk and accompany the individual to casinos in Macau, where they typically provide the gambler with his stake. Almost all junket gamblers play only baccarat, and the casinos' historical statistical win from that game totals 2.85 percent of the "roll" (i.e. the amount bet). The casinos in Macau pay junket operators a commission equal to approximately 1.0 percent of the roll. Therefore, estimating roughly, Macau casinos paid junket operators at least USD 2.1 billion in 2007, calculated as 35 percent (i.e. 1.0/2.85) of the casinos' at least USD 6 billion of win from junket players. The junket operators' wealth and influence dramatically increased in recent years, as Macau's gaming industry boomed.

¶11. (C) The executive in Stanley Ho's group asserted that "all of the junket operators are directly or indirectly

involved with the triads." He criticized the MSARG's recent decision to lift the ceiling on the junket commission rate (from 1 percent to 1.25 percent), which funnels more money to these groups (and, of course, hurts the casinos' bottom lines). Each of our American casino interlocutors stated they only deal with MSARG-licensed junket operators, and that their firms fully comply with U.S. and Macau gaming statutes and regulations. They pointed out their inability to investigate allegations of possible connections between MSARG-licensed junket operators and organized crime, particularly that occurring in the mainland.

¶12. (C) According to Siu, the PRC has become "very concerned" about linkages between Macau's junket operators and organized crime in the mainland. He said the PRC restricted Macau visas for mainlanders, at least in part to stem the rise of organized crime in the mainland associated with the Macau junkets. A senior U.S. executive agreed, and noted that provincial officials in the mainland increasingly provide "sweetheart" deals to junket operators (e.g. land sales, business licenses, government contracts), in exchange for bank deposits or cash sums paid to the officials upon arrival in Macau. He said concerns about corruption and money laundering have also led the PRC to recently "crack down" on money changers that allow a mainland Chinese to pay renminbi in the mainland - whether sourced legally or illegally - and collect the equivalent amount in hard currency in Macau.

¶13. (C) While the junket operators generally avoid direct involvement in illegal activities in Macau, Siu said the companies can easily engage criminals in Macau "to do their dirty work." Siu commented that the Macau police force is "afraid of triad groups" operating there. He said organized crime leaders in Macau "know the identity of each police force member and where they live." According to Siu, this prompted the MSARG to recently request unspecified "enforcement assistance" from Beijing.

#### MSARG's Outdated Hiring Restrictions for Dealers

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¶14. (C) The MSARG mandates that all dealers in casinos be Macanese citizens. Given Macau's significant projected gaming capacity additions, the gaming industry's demand for Macau citizen dealers is expected to significantly outstrip supply. Jay Dee Clayton, Executive Vice President of Operations at Wynn Macau, told EconOff that casino operators will "find it difficult to hire the thousands of entry level dealers this market will need." He said the MSARG's hiring restrictions have started to damage his dealers' career development, as Wynn hesitates to promote its increasingly valuable dealers into middle management. Grant Bowie, President of MGM Grand Macau, agreed. He added that the MSARG's Macau-citizen-only dealer restriction "dumbs down" the citizens of Macau by limiting their promotion opportunities and narrowing the skill sets of Macau's workforce. Macau's 20,000-plus dealers earn an average of USD 1,700 (MOP 13,226) per month. This exceeds Macau's

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median wage by 65 percent. In Macau, high school dropouts earn more as card dealers than new college graduates in nearly every profession.

¶15. (C) Bowie described how the dealer hiring restrictions are negatively affecting a new Small and Medium Enterprise (SME) Initiative begun by AmCham Macau's gaming industry members. Under the initiative, the Big Three American gaming companies (LVS, MGM and Wynn) agreed to foster procurement of goods and services from locally-owned businesses. Bowie said, "But, the SMEs can't find qualified local staff," to produce the goods and services. He said this negatively impacts the local SMEs' ability to deliver products and services in a manner that meets the high demands of U.S. gaming companies.

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